

Message Text

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INFO OCT-01 EA-07 ISO-00 SP-02 USIA-06 AID-05 EB-08
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FM AMEMBASSY MANILA

TO SECSTATE WASHDC PRIORITY 9126

INFO AMEMBASSY WELLINGTON PRIORITY

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USADB

FOR NAC AGENCIES

E. O. 11652: ADS, DECLAS 7/29/77

TAGS: EAID, EFIN

SUBJECT: PROPOSED ADB TECHNICAL ASSISTANCE TO COOK ISLANDS FOR
NATIONAL DEVELOPMENT CORPORATION

SUMMARY: ADB MANAGEMENT PROPOSES \$91,000 TECHNICAL
ASSISTANCE GRANT TO GOVT OF COOK ISLANDS TO FINANCE THE
SERVICES OF A DEVELOPMENT BANKING EXPERT TO HELP ORGANIZE
COUNTRY'S NATIONAL DEVELOPMENT CORPORATION, AND
THE OVERSEAS TRAINING OF TWO INDIVIDUALS FOR MANAGERIAL
RESPONSIBILITIES IN SAME INSTITUTION. USADB SUPPORTS
PROPOSAL. END DSUMMARY.

1. ADB DOCUMENT R40-77 DESCRIBING PROPOSED TECHICAL
ASSISTANCE (TA) GRANT POUCHED ADDRESSEES APRIL 27.
BOARD CONSIDERATION SCHEDULED FOR MAY 17.

2. LOCATED 1,600 KM. EAST OF TONGA AND 4,800 KM. SOUTH
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OF HAWAII, COOK ISLANDS (CI) COMPRISES 15 TINY ISLANDS
DISPERSED OVER 2 MILLION SQ. KM. OF OCEAN. NORTHER
GROUP CONSISTS OF 8 SPARSELY POPULATED AND SUBSISTENCE
ORIENTED CORAL ATOLLS. SOUTHERN GROUP CONSIST OF 7
REEFED, PRIMARILY VOLVANIC ISLANDS, INCLUDING RAROTONGA,
THE SEAT OF GOVERNMENT WITH APPROXIMATELY 51 PERCENT OF
COUNTRY'S 18,000 POPULATION. PREVIOUSLY A TERRITORY OF

NEW ZEALAND (NA), CI IN 1965 BECAME SELF-GOVERNING STATE "IN FREE ASSOCIATION" WITH NZ. UNDER THIS ARRANGEMENT, CI HAS SOLE RESPONSIBILITY FOR INTERNAL AFFAIRS, NZ RETAINS RESPONSIBILITY FOR EXTERNAL AFFAIRS AND DEFENSE.

3. IN PRACTICE, CI AND NZ HAVE CONTINUED TO MAINTAIN EXTREMELY CLOSE ECONOMIC AND COMMERCIAL RELATIONS. NZ CONTINUES TO UNDERWRITE MAJOR PORTION OF CI BUDGET (57 PERCENT IN 1976/77), PROVIDES ONLY SIZEABLE SOURCE OF CAPITAL FUNDS (NZ \$1.7 MILLION OF PROJECT GRANTS IN 1976/77), AND IS VIRTUALLY CI'S SOLE TRADING PARTNER. CI USES NZ CURRENCY AND ITS PEOPLE RETAIN NZ CITIZENSHIP WITH FREE ACCESS TO THAT COUNTRY. EXTENSIVE EMIGRATION FROM CI TO NZ HAS RESULTED IN A NET 3,000 (ONE SEVENTH) REDUCTION OF CI POPULATION SINCE 1971.

4. CI ECONOMY IS BASICALLY AGRARIAN ALTHOUGH GOVT, PARTLY THROUGH ITS EXTENSIVE INVOLVMENT IN COMMERCIAL OPERATIONS, ACCOUNTS FOR LARGEST SINGLE SHARE OF GDP (34 PERCENT) AND IS LARGEST EMPLOYER OF LABOR (51 PERCENT OF LABOR FORCE). PER CAPITA GDP IS ESTIMATED AT NZ \$730 (NZ\$ - U.S. \$0.9569) IN 1975. THIS FIGURE IS CONSIDERABLY INFLATED BY INFLATION OF RECENT YEARS (17.2 PERCENT AVERAGE ANNUAL RATE DURING 1974-76). MOREOVER, IT FAILS TO REFLECT WIDE DISPARITIES IN INCOMES BETWEEN EXPATRAITES AND NATIVE COOK ISLANDERS, AND BETWEEN NORTHERN (ECONMICALLY INACTIVE) AND SOUTHERN COOK ISLANDERS. PRINCIPAL AGRICULTURAL EXPORT CROPS ARE CITRUS, PINEAPPLES, BANNANAS AND COPRA. INDUSTRIAL LIMITED OFFICIAL USE

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ACTIVITY IS CONFINED MAINLY TO FOOD-PROCESSING AND A LIMITED AMOUNT OF LIGHT MANUFACTURING. TOURISM HAS BEEN RAISING SHARPLY SINCE COMPLETION OF RAROTONGA AIRPOT, WITH JET CAPABILITY IN 1973. NUMBER OF OVERSEAS VISITORS ROSE FROM 1,800 IN 1973 TO 9,100 IN 1975, AND IS EXPECTED REACH 20,000 BY 1980.

5. CI EXPORT EARNINGS HAVE DECLINED IN RECENT YEARS, FROM NZ \$2.5 MILLION IN 1973 TO NZ \$2.0 MILLION IN 1976. MEANWHILE, WITH INFLATION AND EXPANSION OF IMPORT-ORIENTED TOURIST INDUSTRY, COUNTRY'S IMPORT BILL HAS RISEN TO APPROXIMATELY NZ \$4.0 MILLION. TRADE DEFICIT IS FINANCED BY ABOUT NZ \$1.0 MILLION OF EMIGRANT REMITTANCES, AS WELL AS TOURISM AND NZ GRANTS. EXPORT DECLINE REFLECTS GENERAL DETERIORATION IN COUNTRY'S AGRICULTURAL SECTOR, ATTRIBUTABLE TO NUMBER OF FACTORS INCLUDING: (I) LACK OF SECTORAL PLANNING; (II) CI'S

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COMPLEX LAND TENURE SYSTEM WHICH HAS LED TO LAND
FRAGMENTATION AND UNDER-UTILIZATION:
(III) EMIGRATION AND CONSEQUENT ABANDONING OF POTENTIALLY
PRODUCTIVE LAND; (IV) LOW RATES OF RETURN TO GROWERS; AND
(V) INEFFICIENT CREDIT FACILITIES. LACK OF RAW MATERIALS,
LIMITED MARKETS (DOMESTIC AND FOREIGN), MANPOWER
SHORTAGE, AND LACK OF INVESTMENT CAPITAL COMBINE TO LIMIT
CI GROWTH POTENTIAL. HOWEVER, BANK MISSION PERCEIVES
SOME OPPORTUNITIES IN AREAS OF AGRO-INDUSTRY AND LIGHT
MANUFACTURING ORIENTED TOWARD NZ MARKET. PRELIMINARY
WORK ON PLANNING HAS BEGUN WITH AID OF CONSULTANT TEAM
UNDER BILATERAL AID FROM NETHERLANDS, AND CONSIDERATION
IS BEING GIVEN TO VIABILITY OF AN INDUSTRIAL ESTATE
IN RAROTONGA.

6. CI BANKING SYSTEM CONSISTS OF ONE LOCAL BRANCH OF
BANK OF NZ WHICH PROVIDES MAINLY SHORT TERM LOANS TO
RETAIL TRADERS AND IMPORTERS. VARIOUS GOVT DEPARTMENTS/
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AGENCIES PROVIDE TERM LOANS, PRINCIPALLY IN HOUSING AND

AGRICULTURAL SECTORS. HOWEVER, BESIDES BEING INADEQUATE TO THE NEED, THEIR OPERATIONS ARE GENERALLY INEFFICIENT, UNRELATED TO PLANNING OBJECTIVES, AND CHARACTERIZED BY HIGHLY UNSATISFACTORY RATES OF LOAN RECOVERY. AS REGARDS DEVELOPMENT FINANCE INSTITUTIONS (DFIS), CI LEGISLATIVE ASSEMBLY APPROVED NATIONAL DEVELOPMENT CORPORATION (NDC) ACT IN MARCH 1975 TO PROMOTE ECONOMIC DEVELOPMENT OF COUNTRY THROUGH PROVISION OF FINANCIAL, MANAGERIAL AND TECHNICAL SERVICES. SEVERAL AMENDMENTS ARE NECESSARY TO PROVIDE NDC THE DESIRED SETUP AND SCOPE AS A DFI. GOVT HAS INDICATED WILLINGNESS TO PROCEED, BUT LITTLE HAS ACTUALLY BEEN DONE FOR LACK OF EXPERTISE IN THIS AREA AND EFFECTIVELY NDC DOES NOT YET EXIST. AS INTERIM MEASURE, CENTRAL PLANNING BUREAU HAS BEEN AUTHORIZED TO RECEIVE LOAN APPLICATIONS WHICH ARE SUBSEQUENTLY CONSIDERED BY AN EXECUTIVE COMMITTEE APPOINTED BY FINANCE MINISTER. AS OF OCT 1976, 12 APPLICATIONS TOTALING NZ \$130,000 HAD BEEN RECEIVED. MISSION CONSIDERS THESE PROCEDURES TO BE INAPPROPRIATE AND UNNECESSARY.

7. MISSION BELIEVES ANY EXPANSION OF ECONOMIC ACTIVITY, PARTICULARLY IN PRIVATE SECTOR, MUST RELY ON AN EFFICIENT CREDIT SYSTEM. NEED IS TO CONSOLIDATE ALL DEVELOPMENT FINANCING OPERATIONS IN ONE CENTRALIZED AUTONOMOUS INSTITUTION, NAMELY NDC. NDC WOULD BE NOT ONLY FINANCING INSTITUTION, BUT WOULD ADVISE GOVT IN ITS ECONOMIC ACTIVITIES, UNDERTAKE PROMOTIONAL ACTIVITIES FOR DEVELOPMENT OF SMALL-SCALE AND COTTAGE INDUSTRIES, AND ACT AS EXECUTING AGENCY FOR SUITABLE DEVELOPMENTAL PROJECTS TO BE FINANCED EITHER BY GOVT OR FOREIGN SOURCES.

8. PROPOSED TA PROVIDES FOR:

(A) PROVISION OF A DEVELOPMENT BANK EXPERT FOR LIMITED OFFICIAL USE

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PERIOD OF ONE YEAR TO BE DESIGNATED, FOR FIRST NINE MONTHS, AS CHIEF EXECUTIVE, AND SUBSEQUENTLY AS ADVISOR. HE WOULD BE RESPONSIBLE FOR ADVISING GOVT ON MATTERS RELATED TO NDC, FOLLOWING UP NECESSARY AMENDMENTS IN NDC ACT, FORMAL ESTABLISHMENT AND ORGANIZATION OF NDC, LAYING DOWN POLICIES AND PROCEDURES, RECRUITMENT AND TRAINING OF LOCAL STAFF, CONSOLIDATION AND TRANSFER TO NDC OF EXISTING LOANS OF OTHER GOVT AGENCIES (AFTER ASSESSMENT OF THEIR QUALITY AND WRITING OFF OF BAD DEBTS, AS APPROPRIATE), AND ASSISTING NDC TO DEVELOP INTO VIABLE, WELL-RUN DFI;

(B) OVERSEAS TRAINING OF TWO INDIVIDUALS, TO BE

SELECTED BY GOVT IN CONSULTATION WITH BANK, FOR SIX MONTHS IN AN ESTABLISHED, BANK-ASSISTED, DFI IN SOUTH PACIFIC (I.E. WESTERN SAMOA OR PAPUA NEW GUINEA). ON COMPLETION OF TRAINING, ONE OF THE TWO WILL BE APPOINTED CHIEF EXECUTIVE OF NDC.

9. EXPATRIATE STAFF TO ASSIST THE CHIEF EXECUTIVE IN THE INITIAL PERIOD AS ACCOUNTANT AND LOAN OFFICER WILL BE PROVIDED UNDER OTHER SOURCES OF BILATERAL AND/OR MULTILATERAL AID. POSSIBILITIES OF ASSISTANCE FROM NZ AND FROM COMMONWEALTH FUND FOR TECHNICAL COOPERATION ARE BEING EXPLORED. BANK EXPECTS COMMITMENTS FOR SUCH ADDITIONAL ASSISTANCE TO BE OBTAINED ALONG WITH PROPOSED TA.

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10. TOTAL COST OF PROPOSED TA IS \$116,000. FOREX PORTION, TO BE FINANCED BY BANK, WOULD BE \$91,000, OF WHICH \$67,000 TO COVER DEVELOPMENT BANKING EXPOERT, \$24,000 TO COVER OVERSEAS TRAINING OF TWO OTHER INDIVIDUALS. GOVT OF CI WILL MEET LOCAL CURRENCY COSTS OF ABOUT \$25,000. COST OF TWO OTHER FOREIGN EXPERTS (PARA. 9) ARE ASSUMED TO BE FINANCED BY NZ GOVT OR COMMONWEALTH FUND FOR TECHNICAL COOPERATION.

11. MISSION PROJECTS TOTAL FINANCIAL ASSISTANCE OF NDC AT NZ \$500,000 IN FIRST YEAR OF NORMAL OPERATIONS, NZ \$600,000 IN SECOND YEAR, NZ \$750,000 IN THIRD YEAR. APPROXIMATELY HALF OF FIRST YEAR CREDITS WOULD BE TO HOUSING REFLECTING LARGE PENT-UP DEMAND IN THAT AREA; 40 PERCENT TO AGRICULTURE; 10 PERCENT TO INDUSTRY AND OTHERS. IN FUTURE YEARS, HOUSING SHARE WOULD TAPER OFF IN FAVOR OF INCREASED REQUIREMENTS OF INDUSTRIAL SECTOR.

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12. CI GOVT WILL PROVIDE EQUITY FUNDS AND SUBORDINATED LONG-TERM LOCAL CURRENCY LOANS TO NDC IN SUITABLE AMOUNTS. GOVT OF NZ ALSO LIKELY TO PROVIDE EQUITY. FORWARD AID PROGRAM OF NZ HAS ALLOTTED NDC NZ \$25,000 IN 1977-78, NZ \$150,000 IN 1978-79, AND NZ REP TO CI HAS INDICATED THAT THESE AMOUNTS MAY BE INCREASED.

13. AT PRESENT, BANK OF NZ PROVIDES TERM LOANS AT 8.5-9.5 PERCENT P.A. LOANS BY EXISTING CI AGENCIES ARE EITHER INTEREST FREE OR AT 3 PERCENT. NDC INTEREST RATE WILL PROBABLY BE LOWER THAN COMMERCIAL BANK (BANK OF NZ) RATE, BUT SHOULD ADEQUATELY REFLECT RELATIVELY HIGH ADMINISTRATIVE EXPENSES IN EARLY PERIOD OF OPERATION. AT SAME TIME, GOVT HAS ASSURED THAT IT WILL PROVIDE ADEQUATE FUNDS IN FORM OF SUBSIDY TO COVER PROVISION FOR BAD DEBTS UNTIL NDC'S OWN INCOME IS ADEQUATE FOR THIS PURPOSE. ON BASIS ESTIMATED LEVEL OF OPERATIONS (PARA. 11), MISSION PROJECTS A SMALL OPERATING PROFIT BY THIRD YEAR OF NDC OPERATIONS. FINANCIAL POSITION WILL BE SATISFACTORY, BASED ON PROPOSED CAPITAL STRUCTURE.

14. ESTABLISHMENT OF A VIABLE DFI APPEARS BEST WAY TO STIMULATE EXPANSION OF PRODUCTIVE CAPACITY WHICH IS SORELY NEEDED TO ARREST DECLINE OF CI ECONOMIC ACTIVITY AND THE STEADY DRAIN OF MANPOWER THROUGH EMIGRATION, AND TO ACCOMMODATE UNSATISFIED NEEDS IN HOUSING AREA. PROPOSED TA WOULD BE BANK'S FIRST PROJECT IN CI AND, AT PRESENT, APPEARS ABOUT ALL THAT BANK CAN DO FOR THAT COUNTRY. IT IS EXPECTED, HOWEVER, THAT ONCE NDC IS FULLY OPERATIVE, IT WILL REPRESENT A SUITABLE MEDIUM THROUGH WHICH FURTHER BANK ASSISTANCE CAN BE CHANNELED. USADB SUPPORTS PROPOSED TA GRANT AND RECOMMENDS FAVORABLE NAC ACTION.

15. REQUEST AMEMBASSY WELLINGTON'S COMMENTS FOR NAC AGENCIES, INFO USADB MANILA, PURSUANT TO STATE 119795 DATED 3 JULY 1972.

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